



Investment Office

P.O. Box 2749

Sacramento, CA 95812-2749

Telecommunications Device for the Deaf - (916) 795-3240

(916) 795-3400

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AGENDA ITEM 6a

TO: MEMBERS OF THE INVESTMENT POLICY SUBCOMMITTEE

- I. SUBJECT:** Investment Office Policy / Delegations Review
Project – Update
- II. PROGRAM:** Total Fund
- III. RECOMMENDATION:** Information
- IV. ANALYSIS:**

The purpose of this item is to update the Subcommittee on the Policy Review Project. Investment Office staff has previously briefed the Subcommittee on this comprehensive project to review, update, and improve upon the existing body of investment policy and delegations. The previous agenda item, which set forth the project objectives, project approach, resources and staffing, and timeline, is provided as Attachment A.

At the Board's request, staff provided at the recent July 2006 Board offsite a briefing on the delegations portion of the project. The objectives of the offsite discussion were to:

- Update the Board on the status of the delegations project, including methodology and findings;
- Engage the Board in a discussion about the purpose, source, and practical application of current Board delegations and to outline considerations to be followed in granting future delegations; and
- Present a path forward with respect to consolidating delegations into a single document for each asset class.

The Board was presented with a matrix summarizing current delegations by subject matter and asset class.

At the offsite, the Board's discussion of delegations was robust and highlighted the significance of this project. The offsite discussion also brought to light issues as to the scope of the delegations project.

Based on the discussion and the guidance received from the Board, and subsequent discussion with the Legal and Compliance Offices, staff is presenting at this time revisions to the scope of the delegations portion of the project, as well as a timeline for moving forward.

Scope of Delegations Project

During the recent offsite, the following questions were raised:

- Will the project include an examination of Investment Committee and Policy Subcommittee charters and delegations?
- Will the project include a review and analysis of "delegations" to consultants, money managers, third party administrators, and other contractors?
- Will the project extend beyond the Investment Program to other CalPERS programs?

The current project is being conducted by the Investment Office and, thus, is limited to the Investment Program. Its scope will include all pertinent delegations in the chain of authority extending from the CalPERS Board of Administration to the Investment Office staff. This will include delegations to the Investment Committee and Policy Subcommittee, and investment-related delegations to the Executive and Investment staff. Currently there are no charters for the Investment Committee and Policy Subcommittees.

Relationships with money managers and other third parties are handled through the contract administration process. For example, the current process for money manager contracts includes a "Letter of Authority," which gives the manager authority to make transactions and execute documents on CalPERS' behalf. These letters, as well as other related contractual provisions, are overseen by the Legal Office. As currently envisioned, the pending policy project will not include an examination of assignments to parties in contractual relationships with CalPERS. The Legal Office will present a future item to the Policy Subcommittee that sets forth the pertinent contractual provisions.

During the course of the discussion it also came to light that a similar exploration of delegations at the enterprise level and in other program areas may also be valuable. We believe this was duly noted by pertinent CalPERS Executive staff present at the offsite.

Path Forward and Timeline for Delegations Project

As explained at the offsite, staff intends to first present to the Policy Subcommittee a set of guidelines or principles to be followed in granting delegations. This will include a definition of “delegation,” as well as technical and substantive considerations for granting delegations. The proposed definition and guidelines will be crafted based on the organic authority for delegations set forth in Government Code section 20099, as well as other pertinent statutory authority, the Board’s existing Governance Principles, input provided by the Board during the offsite, and consultation with appropriate experts.

Following adoption of the guidelines, staff will develop and propose a single comprehensive delegation document for each asset class and will present these to the Policy Subcommittee over a several-month period. A timeline of the agenda items to be brought forward to the Policy Subcommittee is provided as Attachment B. Because of the depth of issues to be discussed, staff suggests that the Subcommittee consider only one or two asset classes per meeting. Since the Subcommittee’s regularly scheduled meetings are every other month, this process will take several months. Upon approval by the Subcommittee, each item would then be brought to the full Investment Committee.

The review of each asset class will include a review of existing delegations, proposed changes based on the new guidelines, recommended changes in the delegations themselves, and changes to address any other issues brought to light through the Project. In consideration of the input received from the Board at the offsite, the upcoming discussions will highlight the finality of decision-making authority; Board reporting and monitoring requirements; best practices where applicable; and restrictions on the authority to re-delegate.

Once the new delegation documents are in place, a disciplined process will be used to maintain a consistent and transparent body of delegations. In addition, staff suggests that the Investment Committee undertake a periodic review (e.g., every other year) of the full body of delegations.

Path Forward for the Policy Review Portion of the Project

As noted above, we have completed the discovery and analysis phases of the *delegation* portion of the Policy Review Project. Over the next several months we will implement the results of this effort with discussions before the Policy Subcommittee and the full Investment Committee.

During this same time frame, we will launch the discovery and analysis phases of the *policy* portion of the project. We will review the existing inventory of all CalPERS investment policy, and array the results of these findings by subject/purpose. We will examine intent, determine if there are apparent gaps in practice versus policy, review format and clarity, and report our initial findings in an appropriate forum (possibly the January Board offsite). At that time, working with our Compliance Office, we will bring forth a set of recommendations to streamline current and future investment policy. A more definitive timeline for this portion of the project will be presented at the October Policy Subcommittee meeting.

V. STRATEGIC PLAN:

This item supports:

- Goal VIII: Manage the risk and volatility of assets and liabilities to ensure sufficient funds are available, first to pay benefits, and second, to minimize and stabilize contributions; and
- Goal IX: Achieve long-term, sustainable, risk-adjusted returns.

VI. RESULTS/COSTS:

Upon completion of this project, the CalPERS Investment Program will have a streamlined policy and delegations framework that is clear, consistent, and accessible. This will allow the Investment Committee, Investment Policy Subcommittee, and Investment Office staff to operate within a transparent and clearly stated body of delegations that set forth a clearly defined chain of authority and responsibility, along with standards for monitoring and reporting. The results of this project will also serve as a foundation for future delegations and policy decisions.

This project will require substantial staff and consultant resources. Wilshire and PCA consultant services for this project fall within the scope of existing contracts. The cost for services provided by The Results Group will be absorbed within the existing budget.